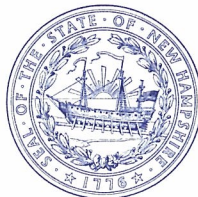


THE STATE OF NEW HAMPSHIRE

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December 3, 2009



Debra A. Howland
Executive Director
New Hampshire Public Utilities Commission
21 S. Fruit St., Suite 10
Concord, New Hampshire 03301

Re: DG 08-009, Energy North Natural Gas, Inc. d/b/a National Grid NH
Petition for Rate Increase
Staff Report Re: Rate Case Expense Review

Dear Ms. Howland:

This letter provides recommendations regarding the recovery of rate case expenses by EnergyNorth Natural Gas, Inc. d/b/a National Grid NH (the Company) in this docket and describes Staff's assessment in connection with the recommendations. Except as otherwise noted, the opinions expressed herein are those of Staff.

On June 26, 2009, the Company filed a summary of rate case expenses and supporting documentation for review by Staff and the Office of the Consumer Advocate (OCA). In that filing the Company's rate case expense summary totaled \$779,038. On August 19, 2009, the Company notified Staff that rate case expenses totaled \$802,635, including Miscellaneous Expenses of \$23,597 contained in the supporting documentation that had been inadvertently omitted from the rate case expense total. On October 15, 2009, Audit Staff issued its audit report regarding rate case expenses, confirming that Miscellaneous Expenses had been omitted in the total but reducing those expenses by \$1,541 to correct for a Company error. The Audit Report concluded that rate case expenses of \$801,094 were materially accurate based on its review of the supporting documents and Company audit responses. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 25,032 (October 29, 2009) approved the inclusion of \$802,365 of rate case expenses in the 2009-2010 Local Distribution Adjustment clause (LDAC) rate, subject to final review and approval. *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 25,044 (November 13, 2009) denied the Company's motion for rehearing and/or reconsideration of Order No. 24,972 (May 29, 2009) (order approving an increase in permanent rates).

Staff and the OCA issued numerous data requests to the Company regarding the rate case expense filing. Areas investigated included the Company's procurement policies and procedures regarding the retention of outside service providers, the contractual arrangements made for the consultants and attorneys used in this docket, expense reimbursement policies for Company employees, adherence to the Company's policies and the contracts, and details regarding specific expenses.

Staff, OCA and the Company (Parties and Staff) met on November 10, 2009 to discuss the Company's data responses and explore the potential for settlement. While there are differences of opinion regarding the necessity, amount and/or reasonableness of certain expenses among Parties and Staff, they agreed as a compromise of all rate case expense issues to recommend that the Company be allowed to recover a total of \$788,416 in rate case expenses, a reduction of \$14,219 from the amount originally requested. In addition, the Company will not seek to recover any rate case expenses related its motion for rehearing (McLane invoices dated July 6, 2009 through November 11, 2009, totaling approximately \$36,500).

With this reduction, ratepayers will only be charged standard transportation costs incurred by Company personnel and will not be charged for alcohol, legal fees billed above 2008 hourly rates, legal fees and expenses incurred to date related to the Company's motion for rehearing, and expenses related to the Commission audit. The Company retains the right to seek recovery of future rate case expenses related to its response (if any) to the Commission denial of its motion for rehearing; however, if recovery of such expenses is requested, the other parties are free to take whatever position(s) they believe are appropriate.

In addition, the Company agreed, upon request of a party at an early stage of the next rate case, to provide the Staff and parties (i) evidence that the Company's procurement policies and procedures have been complied with and that these policies and procedures are no less strict than those currently in effect (PP-303S for competitively bid procurements and PP 307 for any non-competitive procurements) and (ii) copies of the contracts with outside consultants and attorneys upon which claims for rate case expense recovery will be based.

This compromise resolution of rate case expenses is the product of settlement negotiations. Accordingly, the content of such negotiations is privileged and all offers of settlement are without prejudice to the positions of the Parties and Staff in any future proceedings. It is also understood that the Commission's acceptance of this recommendation does not constitute precedent or an admission by the Parties or Staff in any future proceeding.

The rate case expenses in this case are substantial. For purposes of this case, Staff accepts the Company's decision to obtain the services of outside consultants and attorneys. Staff notes, however, that some large utilities, such as Public Service Company of New Hampshire, choose to do all or substantially all of the work in-house and even if the choice to use outside services is made, utilities need to carefully consider

the extent to which outside service should be relied on when ratepayer recovery of the costs is sought.

In Staff's view, obtaining competitive bids from outside consultants and attorneys can be an important element in containing rate case expense, and the results of competitive bidding can provide an objective basis upon which to evaluate the reasonableness of rate case expenses. Indeed, the Company's procurement policies and procedures appropriately reflect the desirability of competitive bidding in most cases. In Staff's view, the Company's policies and procedures for competitively bid procurements and non-competitive procurements are reasonable and, if strictly adhered to, should help ensure that rate case expenses approved for ratepayer recovery are prudently incurred and reasonable in amount. For procurements of \$10,000 or more, those policies and procedures require the Company to "seek competitive bids (and acceptance of the lowest compliant bid) whenever possible, except where compelling reasons exist for single source action." The policies and procedures further require the Company to justify a non-competitive procurement in writing and to have a person with requisite Delegation of Authority (DOA) authority approve the non-competitive procurement in advance. Once single source status is approved, the Company's purchasing agent is to negotiate pricing and other terms.

The Company engaged outside contractors on a competitive bid basis to provide rate case services for depreciation, revenue and expense lead/lag, marginal costs/rate design and cost of equity. Two firms, the McLane Law Firm (McLane) and Hewitt Associates (Hewitt), were engaged on sole source procurements. McLane's rate case expenses totaled \$411,812 and Hewitt's totaled \$13,485.

Staff does not question the Company's decision to engage McLane or Hewitt in this case. Pursuant to the settlement agreement approved in *EnergyNorth Natural Gas, Inc. d/b/a National Grid NH*, Order No. 24,777 (July 12, 2007), the Company was required to file a base rate case within six months of the closing of the merger of KeySpan Corporation and the Company's corporate parents, i.e., by late February, 2008. Given the short amount of time after the merger in which the rate case was to be filed and McLane's and Hewitt's "historic knowledge of and familiarity with the Company and the relevant legal, regulatory and other issues,"¹ there was, in Staff's view, an adequate basis for engaging them on a sole source basis. Nevertheless, Staff is concerned that the Company did not follow its policies and procedures of justifying the non-competitive procurements in writing and having a person with DOA authority approve the non-competitive procurements in advance of the engagements.

The Company engaged Hewitt to provide services related to the Company's pension plan pursuant to a general purpose engagement letter dated January 28, 2008. The Company engaged McLane pursuant to an engagement letter dated February 13, 2003 between McLane and KeySpan Corporation and its subsidiaries; certain terms of the engagement were set forth in KeySpan Corporation's Guidelines for Outside Counsel attached to the letter. Among other things, the Guidelines specified that "[e]very

¹ See the Company's response to Staff rate case data request 1-4.

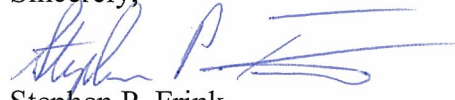
engagement . . . of outside counsel in which the fees for the entire matter are expected to exceed \$25,000 should be memorialized by a letter setting forth the terms and conditions of the engagement in a form acceptable to KeySpan.” The Company did not execute a separate engagement letter as contemplated by the Guidelines.

Staff is concerned that because the Company did not obtain a separate engagement letter with pricing and other terms specific to the rate case, the Company failed to take advantage of an opportunity to negotiate the terms with the specific goal of containing and controlling rate case expenses. In addition, Staff is concerned that the terms of an engagement of this magnitude be clearly and completely documented before the engagement commences.

Regarding future rate filings, Staff and the OCA strongly encourage the Company to obtain and retain itemized receipts, not merely the credit card receipts required by the Company’s expense reimbursement policy, in order to be able to demonstrate that such costs were prudently incurred and reasonable in amount. In addition, Staff and the OCA strongly encourage the Company to provide with their rate case expense filing copies of all invoices for outside rate case services based in whole or in part on hourly rate billing that detail the number of hours billed, the billing rate, and the specific nature of the services performed. Finally, Staff and the OCA expect the Company to be prepared to document and justify any ground transportation costs beyond the costs of buses or car rentals.

Staff recommends that the current LDAC rate remain in effect, as there is not a material difference between the \$788,416 of rate case expenses recommended for approval and the estimated rate case expenses of \$802,365 used in calculating the LDAC rate. Rate case expense recoveries would be reconciled with the approved rate case expense amount and the resulting over/under-recovery would be addressed as part of the Company’s 2010-2011 winter cost of gas proceeding.

Sincerely,



Stephen P. Frink

Assistant Director, Gas & Water Division

cc: Service List